

Assembly Bill 2831

CALIFORNIA COMMUNITY DEVELOPMENT FINANCIAL INSTITUTION TAX CREDIT AND CERTIFICATION PROGRAM

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ISSUE

The California Community Development Financial Institution (CDFI) Tax Credit and Certification Program were initiated in 1997, and have been administered by the California Organized Investment Network (COIN), within the California Department of Insurance. COIN administers the CDFI program by certifying CDFIs that wish to receive qualified investments, and certifying the tax credits for investors.

CDFIs are mission-driven community organizations, separate from government control, dedicated to providing financial products and services to low-income communities underserved by traditional financial markets.

They serve a critical role in addressing issues of poverty and access to credit by providing development services or technical assistance to their borrowers along with the loans and investments they make. CDFIs may be community development banks, loan funds, credit unions, microenterprise funds, corporation-based lenders, or venture funds.

Under current law, this program will sunset on January 1, 2007. This measure seeks to extend the sunset date to January 1, 2012.

EXISTING LAW

The current CDFI Tax Credit and Certification Program are governed by Revenue and Taxation Code Sections 12209, 18053.57, and 23657.

- Authorizes the CDFI Tax Credit and Certification Program, administered by COIN in the California

Department of Insurance, until January 1, 2007.

- Allows a tax credit in the year the investment was made equal to 20 percent of the amount of each qualified investment made by a taxpayer.
- Specifies the certification guidelines and requirements for the Department, the CDFI, and investors.
- Provides for tax credits in an aggregate amount not to exceed \$2 million annually for qualifying investments totaling \$10 million.

THIS BILL

The intent of this bill is to authorize the Insurance Commissioner to develop instructions, procedures, standards, and regulations to administer the CDFI Tax Credit and Certification Program.

- Extends the program sunset date from 2007 to 2012.
- Makes changes related to the certification of CDFIs and investors in connection with certifying the tax credits. To encourage a broad distribution amongst the CDFIs and equitable access to the program by both small and large participants, it would:
 - Establish an annual limit for total qualified investments used by a single CDFI.
 - Establish a set aside for smaller investments to make sure that smaller CDFIs and investors have

the opportunity to utilize the program.

- Provide a set aside to encourage the insurance industry to participate in community development investing.
- Requires CDFIs to report their program information to the Department every other year. The Department will then report the information to the Legislature.
- Requires the Legislative Analyst to evaluate the program with a report to the Legislature in 2010.

SUMMARY

This bill:

- Continues the CDFI program;
- Modifies the certification process for CDFIs and investors.
- Requires a report be sent to the Legislature every other year on the CDFIs use of the tax credit program and a Legislative Analyst evaluation of the program in 2010.

FAQs

What is a CDFI?

CDFI stands for "Community Development Financial Institution". CDFIs are community organizations, separate from government control, which revitalize disadvantaged areas and provide economic opportunities for low-income people. They provide development services or technical assistance to their borrowers along with the loans and investments they make for community and economic development. A CDFI may include a community development bank, loan fund, credit union,

micro-enterprise fund, corporation-based lender or venture fund.

How does a CDFI obtain certification?

A CDFI can obtain certification by COIN as a California CDFI by demonstrating that:

- 1) it is a private financial institution located in this State;
- 2) its primary mission is community development;
- 3) it lends in urban, rural, or reservation-based communities in this State.

What is a qualified investment?

A qualified investment is an investment in a CDFI that is:

- 1) a deposit or loan that does not earn interest; or
- 2) an equity investment; or
- 3) an equity-like debt instrument that conforms to the specifications for these instruments as prescribed by the U.S. Department of the Treasury CDFI Fund, or its successor.

All qualified investments must be equal to or greater than \$50,000 and, for a minimum of sixty (60) months, qualify for a 20 percent tax credit during the year in which the investment was made.

Who can make qualified investment?

Any individual, partnership or corporation with a valid tax identification number is eligible to make a qualified investment. As of January 1, 2000, insurers were eligible to make qualified investments in exchange for a premium tax credit. Additionally, qualified investments made by foreign insurers will not be negated by a state's retaliatory law in the event that a foreign insurer's home state has a premium tax in excess of California's 2.35 percent.

What happens when a taxpayer makes a qualified investment?

The CDFI reports the investment to COIN along with information identifying the taxpayer and substantiating that the investment qualifies. COIN provides a tax credit certificate to the taxpayer with a copy to the CDFI and annually reports the tax credits certified to the Franchise Tax Board and the Board of Equalization.

What happens if the taxpayer withdraws or reduces the investment before the end of the 60 month term?

The CDFI is required to report either event to COIN and the appropriate taxing authority. For withdrawals or reductions bringing the investment below \$50,000 where the withdrawn funds are not reinvested in another CDFI within 60 days, the entire amount of the tax credit is lost and will be added to the net tax for the taxable year in which the withdrawal occurs. For reductions bringing the amount to no less than \$50,000, the amount of the tax credit related to the amount of the reduction (i.e., 20% of the amount of the reduction) is lost and will be added to the net tax for the taxable year in which the reduction is made.

BACKGROUND

The California Community Development Financial Institution (CDFI) Tax Credit and Certification Program have become well-known and established with both CDFIs and investors such that the demand far exceeds the supply of tax credits. There are now 78 certified CDFIs in the State. This represents a 66 percent increase from the 47 that were certified when SB 409 was introduced in 2001 to last extend the program.

In this era of more limited government and foundation funding, CDFIs have increasingly found this modest State incentive to be an invaluable means to attract and leverage additional private capital investments to fund initiatives to address the growing gap that exists between the financial products

and services available to the economic mainstream and those offered to low-income communities.

In calendar year 2005, the program was so popular with investors and CDFIs that the entire annual amount available for tax credits was exhausted by 11 proposals received in January. In 2006, four investments were received on the first business day of the calendar year that represented 80 percent of the total annual amount available.

Now that the program is expected to be oversubscribed each year, this bill seeks to put in place mechanisms to encourage a broad distribution and equitable access to the program by both small and large participants. It would also provide a set aside to encourage the insurance industry to participate in community development investing, given that they do not enjoy the same incentives as other financial institutions, such as banks.

The program provides for a one-year, 20 percent tax credit for qualified investments of \$50,000 or more made for a minimum of five years in CDFIs. The program was expanded in 2000 to make insurers eligible to make qualified investments in exchange for a premium tax credit.

RELATED LEGISLATION

- **SB 409 (Vincent, Ch. 535, Stats. 2001)**
Expanded and clarified the definition of qualified investments, extended the tax credit program for five additional years, and provided carry-over of any unused credit to future years.
- **AB 145 (Vincent, Ch. 821, Stats. 1999)**
Expanded the program to make insurers eligible to make qualified deposits or equity investments in exchange for a premium tax credit.

▪ **AB 1520 (Vincent, Ch. 947, Stats. 1997)**

Provided for a one-year 20 percent tax credit for qualified deposits of \$50,000 or more in California CDFIs.

SUPPORT

John Garamendi, Insurance Commissioner
(Sponsor)
Association of California Insurance
Companies
Bridge Housing
California Association for Local Economic
Development
California Community Economic
Development Association
Clearinghouse CDFI
El Futuro Credit Union
EmTek Fund
Lenders for Community Development
Local Initiatives Support Corporation
Los Angeles Neighborhood Housing Service
Low Income Investment Fund
Mission Community Bank
National Cooperative Bank Development
Corporation
Nehemiah Community Reinvestment Fund
Neighborhood Housing Services of Orange
County
Northern California Community Loan Fund
Opportunity Finance Network
Pacific Association of Domestic Insurance
Companies
Pacific Coast Regional
Peoples Community Partnership Federal
Credit Union
Personal Insurance Federation of California
Renaissance Entrepreneurship Center
Rural Community Assistance Corporation
San Diego Housing Federation
San Fernando Valley Economic
Development Center
San Luis Obispo County Housing Trust
Fund
South County Housing Corporation
State Assistance Fund for Enterprise,
Business and Industrial Development
Corporation
TELACU
Western Financial Bank

Housing California

OPPOSITION

Department of Finance

STATUS

Passed the Assembly Floor (concurrence)
(vote 79-0).

Passed the Senate Floor (vote 40-0).

Passed the Senate Committee on
Appropriations (vote 13-0).

Passed Senate Revenue and Taxation
Committee (vote 7-0).

Passed Assembly Floor (vote 80-0).

Passed Assembly Appropriations
Committee (vote 18-0).

Passed Assembly Revenue and Taxation
Committee (vote 7-0).

FOR MORE INFORMATION

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